

**ORAL TESTIMONY OF
COMMISSIONER OF INTERNAL REVENUE
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BEFORE THE HOUSE GOVERNMENT REFORM
SUBCOMMITTEE ON REGULATORY REFORM
HEARING ON
PAPERWORK BURDEN REDUCTION
MAY 25, 2005**

Madam Chairman, Mr. Lynch, and Members of the Subcommittee, thank you for the opportunity to testify on the Internal Revenue Service's efforts to reduce unnecessary paperwork burdens on the taxpayer.

As this committee well knows, individuals and businesses spend more than six billion hours a year on tax paperwork and other tax challenges. Together, the Internal Revenue Code and regulations run for millions of words. In terms of pages, that's twice as many pages as twenty years ago.

Burden is a direct result of the complexity of the Code. And not only does complexity cause economic burden, it also obscures understanding. Complexity in the tax code compromises both our service and enforcement missions. Taxpayers who seek to comply but cannot understand their tax obligations may make inadvertent errors or may ultimately throw up their

hands and say “why bother.” In the enforcement context, complexity facilitates behaviors at variance with those intended by Congress.

Our goal is to impose the least amount of burden necessary for taxpayers to meet their tax responsibilities. A certain amount of paperwork, of course, is essential to tax collection. Taxpayers must report what they make to the IRS. Their incomes and businesses can be complex. Their deductions and credits can be complex. So the paperwork can be complex. That having been said, we seek to reduce unnecessary paperwork and make the filing process as simple and convenient as possible.

The Office of Taxpayer Burden Reduction at the IRS has aggressively pursued burden reduction initiatives. Since the office was launched in January 2002, we have reduced taxpayer burden by over 200 million hours.

One area of our initiatives involves filing thresholds. We recently increased the Federal Unemployment Tax (FUTA) deposit threshold from \$100 to \$500, reducing burden for over 2.6 million employers. We also increased the threshold for filing Form 1040EZ and Form 1040A from \$50,000 to \$100,000, decreasing taxpayer burden by more than 5 million hours. And

for small businesses, we increased the threshold for business expenses reported on the Form 1040 Schedule C-EZ from \$2,500 to \$5,000. This enabled about 500,000 more taxpayers to file the Schedule C-EZ instead of the Schedule C.

We are also working to reduce burden through other means. For example, we are simplifying forms and instructions. We simplified the Schedules K-1 for partnerships and S corporations, reducing burden by an estimated 95 million hours for the 20 million taxpayers who file these forms. In addition, we are actively considering allowing very small employers to file their employment tax returns annually instead of quarterly. We estimate that this action alone could reduce burden on approximately 1 million businesses by 51 million hours.

The revolution in electronic filing also helps to reduce the paperwork burden. Electronic filing of taxes requires less paper and is more accurate. Computers catch mistakes that would have been made on paper and required more time to correct. This year, for the first time, more than half of all individual taxpayers have filed electronically. Starting next year, we

have mandated that all larger companies file electronically. This will reduce significant amounts of paperwork and speed up audits.

Congress has a key role in reducing the paperwork burden. Dealing with complexity and paperwork is easier if the tax code is stable. But tax laws change quite frequently. For example, take the American Jobs Creation Act. The Jobs Act brings important benefits to the economy and does much to strengthen the Government's hand in combating abusive shelters. But the new law also adds a lot of complexity to the code. The Jobs Act has 193 provisions; 178 of these require IRS actions like the issuance of guidance and new forms.

Before I close, let me briefly discuss tax reform, the real opportunity for significant simplification and burden reduction. Earlier this year, the President created a bipartisan panel to examine ways to "simplify Federal tax laws to reduce the costs and administrative burdens of compliance with such laws." In March, I appeared before the panel and made five suggestions concerning tax reform.

- First, our economy is constantly evolving, with change seemingly ever accelerating. Examples of change include transformation of the workforce to more self-employed individuals; businesses contracting out activities they'd previously done themselves; the relatively greater portion of economic growth generated through smaller, non-manufacturing businesses; and increasing globalization. It is vital to construct a tax system that recognizes this dynamic and is built for the 21st Century, not the 1960s.
- Second, policy options should be carefully assessed for their potential impact on attitudes towards compliance. Fairness and the perception of fairness are essential, as the President has recognized in his charge that reform proposals be “appropriately progressive.”
- Third, administerability is also an important consideration. Bolting on new programs to the tax code without significantly simplifying or eliminating existing elements may in fact make it more difficult to collect the \$2 trillion we need to fund the Government.

- Fourth, there needs to be an apples-to-apples comparison. We should not compare a sub-optimized existing system to a perfect, theoretical system. I can assure you from my conversations with counterpart tax administrators that there are administrative and compliance issues in all systems.
- Finally, we must recognize that transition issues associated with migration to a new system, or systems, merit close attention. If the transition is not properly planned and managed, the new system will get off to a rocky start. After such a start, it may take decades to recover.

I wish to emphasize that these points are not offered to suggest inaction. That would be perhaps the worst option. I strongly support the President's call for simplification. Simplification is essential to burden reduction.

Thank you.